



City of Philadelphia  
Office of the City Controller

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## Office of the City Controller Finds Minimal Improvement to Financial Management and Prior Year Findings in Report on Internal Control and On Compliance and Other Matters

*Audit identifies two material weaknesses and seven significant deficiencies.*

**Philadelphia, PA** – The Office of the City Controller released the Report on Internal Control and On Compliance and Other Matters Fiscal Year 2018, finding that the City had two material weaknesses and seven significant deficiencies in its internal control over financial reporting.

“Year after year, the City has multiple serious deficiencies in its internal controls over financial reporting and year after year, they take minimal action to address them. While progress was made on the Treasurer’s reconciliation issues, the City has not made a concerted effort to address most of the other findings,” said City Controller Rebecca Rhynhart. “The City of Philadelphia continues to be the worst among the top ten cities as it relates to internal controls. I’m urging the finance director and the mayor to treat these findings with the urgency they deserve so that taxpayer money is not at risk.”

The fiscal year 2018 (FY2018) report identified findings similar to the fiscal year 2017 (FY2017) report, which identified two material weaknesses and eight significant deficiencies. Over the course of the fiscal year, only one of the 10 findings was resolved completely. Progress was also made on Treasurer’s Office reconciliation procedures, which was a material weakness in FY2017, but is cited as a significant deficiency in FY2018, however issues with reconciliations persist. In addition, a new material weakness and a new significant deficiency were also identified in FY18’s report.

A material weakness is a deficiency, or combination of deficiencies, in internal control resulting in a reasonable possibility that a material misstatement of the City’s financial statements may not be prevented or detected and corrected on a timely basis. For FY2018, the following material weaknesses were identified.

**Material weakness: Inadequate staffing levels, lack of technological investment and insufficient oversight led to undetected material misstatements in the preparation of the City’s Comprehensive Annual Financial Report (CAFR).**

While the City’s financial statements were presented fairly, in all material respects, the Controller’s Office found that Finance Office staff did not detect \$236 million in errors, including \$122.4 million in material misstatements in the Aviation Fund financial statements that were not identified by Aviation or Finance accountants during the preparation of the FY2018 Comprehensive Annual Financial Report. Auditors from the Controller’s Office

identified the errors during their review and notified Finance accountants who, subsequently, corrected most, but not all of the errors. The Controller's Office found that a 28 percent decrease in accounting staff since 2000, including a decrease of one full-time employee over FY2017 totals, as well as the lack of a comprehensive financial reporting system are the cause for this finding. Errors in the CAFR preparation have been a finding in the internal control report since FY2007 without remediation. The Controller's Office recommended that the Finance Office move forward with its plan to use an accounting firm to assist with the preparation of the CAFR in the short-term. However, Finance Office management should either hire more accountants, or invest in a new financial reporting system that will reduce the labor-intensive procedures needed to prepare the city's CAFR as a long-term resolution.

**Material weakness: Untimely and inaccurate preparation of the Schedule of Expenditures of Federal Awards (SEFA) resulted in the late submission of the single audit reporting package to the Federal Audit Clearinghouse.**

The Finance Office's Grants Accounting and Administrative Unit (GAAU), which is responsible for preparing the SEFA, did not prepare and provide for audit a preliminary SEFA until 13 days before the submission deadline. Additionally, the provided SEFA was inaccurate. As a result, the city did not submit a single audit reporting package to the Federal Audit Clearinghouse by the federally required deadline. The late submission of this information could negatively impact the city's receipt of state and federal grants. The Controller's Office recommended that the Finance Office's GAAU allocate adequate resources to ensure the timely preparation and submission of an accurate SEFA for audit purposes and proactively enforce the existing policies and procedures requiring departments to complete expenditure reconciliations by the due date.

A significant deficiency, while less severe than a material weakness, is a deficiency, or a combination of deficiencies, that warrants attention. For FY2018, the following significant deficiencies were identified:

- Remaining deficiencies in Treasurer's Office bank reconciliation procedures still create potential for undetected errors and irregularities;
- Failure to close out prior year grant activity increases risk of reporting errors;
- Failure to segregate payroll duties could allow fraud to occur;
- Capital asset control deficiencies increase risk of reporting errors;
- Failure to timely transfer funds between city bank accounts could result in significant reporting errors;
- Lax monitoring of adjustments to tax accounts may lead to undetected errors or irregularities; and
- Standard Accounting Procedures (SAPs) require updating to ensure accurate and consistent application of accounting rules and regulations.

Of note, deficiencies in the Treasurer's Office bank reconciliations procedures is now a significant deficiency. In last year's report, it was identified as a material weakness and resulted in a \$33.3 million variance (as of June 30, 2017). Over the course of the fiscal year, the Treasurer's Office took steps to address the reconciliation issues and reduce the unknown variance. Improvements were made, however, reconciliation issues persist. The remaining variance, \$529,000 (as of June 30, 2018), has not yet been identified, an additional \$13.5 million in bank receipts remain unmatched, and appropriate supporting documentation was not provided to the audit staff to verify the reconciliation process was performed properly for four of the long unreconciled accounts.

Further details on the significant deficiencies are outlined in the full [report](#), as well as the administration's response and the Office of the City Controller's comments on the administration's response, are available in the report. A quick guide for the report can be viewed [here](#).